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Chadian Oil: Avoiding the Resource Curse

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Abstract:

All too often the benefits of natural resources are not realized by the portions of the population most in need. As has been seen time and time again, revenues from resources such as oil are mismanaged, or worse embezzled, by governments either unable or unwilling to dedicate the funds to issues such as poverty, health care, and education. As Chad begins to exploit the oil resources it has become a “model” for how revenues should be managed, due to a groundbreaking agreement between the government, oil companies, and the World Bank. This model is in jeopardy of failing, however, as the government of Chad is attempting to amend crucial legislation regarding oil revenues and their uses.

Introduction

According to an article in *The Economist* on September 17, 2005, Norway was once again named by the United Nations as the best country in the world in which to live. The article goes on to describe the low unemployment, high wages, and free education that Norwegians are able to enjoy. The author declares that this “enviable lifestyle is largely bankrolled by North Sea oil (*Economist* 9/17/05, 51).” Unfortunately Norway seems to be the exception to the rule when it comes to managing its oil revenues in a way that truly benefits its citizens. In country after country, from Nigeria, Angola, and the Sudan to Saudi Arabia and Iraq for example, there have been clear disparities between national oil revenues and spending on social programs. In these countries, irresponsible spending and corruption have proven a failure by governments to provide for their citizens. The recent exploitation of oil in Chad represents a new opportunity for the international community to ensure that natural resource revenues are managed effectively.

Oil, like other resources, should be a source of revenue and opportunity for countries. However, as has been hinted, these opportunities are often not realized. This is thought to be caused by what is known as the “resource curse.” According to Ian Gary, “The ‘paradox of plenty’ or ‘resource curse’ are phrases academics use to describe the tragic gap between the promise of petroleum and the perversity of its performance (Gary 6/05, 36).” Gary goes on to claim that “...the dramatic development failures by most oil-dependent countries reveal that petrodollars have not helped developing countries reduce poverty. In many cases, they have actually exacerbated it (Gary, 36).” The term “resource curse” is misleading, as it seems to spell doom for those who are, or are in the process of, exploiting valuable natural resources. Another example of a resource that can often (though unnecessarily) lead to problems rather than solutions is that of diamonds. Diamonds are a valuable resource, and the revenues that come from them could be used to help solve issues of poverty, education, and health care in poor countries. However, time after time, it has been shown that diamonds can lead to more problems than they are worth, hence the term “conflict diamonds.”

In the book *Natural Resources and Violent Conflict: Options and Actions*, published in 2003 by the World Bank, Michael Ross describes the natural resource curse, and “how wealth can make you poor (Bannon 2003, 17).” Ross is quick to point out that natural resources are never the only source of a conflict. He states that “any given conflict is brought about by a complex set of events; often poverty, ethnic or religious grievances, and unstable governments also play major roles (Bannon, 19).” He also claims that resources do not make conflict inevitable and for every resource conflict, there are two or three countries that have avoided one. Because unstable governments can play an inadvertently important role in resource conflicts, Ross feels “better policies may help to reduce the likelihood that resources will generate conflict and to direct resource wealth instead to education, health, and poverty reduction (Bannon, 19).”

Echoing Gary, Ross cites a growth in poverty as one of the two economic circumstances that can result from resource dependence. The other circumstance is a reduction of economic growth, as resource dependent economies grow slower than others. Ross finds a correlation between poverty and resource dependence because of what he claims is “an unusually poor job of providing education and health care for their citizens (Bannon, 20).” For example, Ross finds a “strong correlation between greater independence on oil and mineral exports and higher child mortality rates: for each increase in mineral dependence of five points, the mortality rate for children under the age of five rose 12.7 per 1,000; for each five point increase in oil dependence, the under-five mortality rose 3.8 per 1,000 (Bannon, 20).” Corruption is also a very damaging reality in these countries that lack strong oversight capacity. For example, according to Thilo Thielke, in the article “The Race for Resources: Gangsters and Africa’s Black Gold Rush” in *DER SPIEGEL* magazine, “In the past three decades alone, fossil fuel has allegedly brought more than \$280 billion dollars into Nigeria. Most of this has disappeared into the pockets of corrupt politicians (Thielke 12/7/05).”

Resources like oil and diamonds are not inherently a “curse.” In fact, as has been shown in Norway, oil can provide great opportunities for a country. When oil was discovered in Chad, it was seen by the international community as an opportunity to bring one of the poorest nations in the world out of the depths of despair. When oil production began in late 2003, Chad was ranked 165th out of 175 countries on the United Nations Development Programme’s Human Development Index (Paulus 10/13/03). However, in order for Chad to truly realize the potential of the projected \$80 million dollar annual oil revenues, it must come to grips with both its past, and what it needs to do for the future (Paulus 10/13/03). Good governance and corporate social responsibility need to play prominent roles in this development project.

In order to understand Chad’s current economic, social, and political predicaments, it is necessary to know a little about its history. First of all, Chad is a large, landlocked, state in northern Africa. It is mostly desert, with some fertile areas in the extreme southern part of the country. Its population of 9.5 million is 51% Muslim (mostly in the north) and 35% Christian (mostly in the south), and it speaks mostly French and Arabic (U.S. State Dept. 10/05). Chad gained official French colonial status in 1920, and as a colony, it suffered the fate of most African countries. The French colonial policies caused “regional disparities, stagnation, and decline in food productivity; impoverishment from taxation and forced labor; and a decline in social cohesion and communalism (Azevedo 1998, 31).”

Chad gained independence on April 11, 1960. Five years later a civil war broke out between the Muslims of the north and east, against the southern-based government. This conflict continued for almost 40 years in various forms and alliances (State Dept. 10/05). For those 40 years spending by the government was focused on military expenditures, instead of on social services. For example, in 1986, Chadian military expenditure was between 5 and 10 percent of the GNP; however health and education only constituted 2 percent (Azevedo, 82). This civil war was devastating not only socially, but economically as well. The war “also caused considerable economic decline in investment, disappearance of industries, disruption of international trade, massive corruption, and looting of the national treasury (Azevedo, 82).”

By 2003 relative stability had been regained by the government and work had been done on rebuilding the economy. However, foreign aid remained the backbone of Chad’s economy, as the country was unable to provide for itself (Azevedo, 82). So one need only envision a country that is mostly desert, inhabited by subsistence farmers, torn by four decades of civil war, which has a government riddled with corruption and abuse. This is Chad.

Oil exploitation in this unstable country began in the southern Doba region in June of 2000, and continued as a result of an ExxonMobil based consortium, which, along with the World Bank, has invested \$3.7 billion dollars into the project (Paulus 10/13/03). The discovery of oil in Chad was no accident. According to Gary, “with declining production in Europe and North America and dwindling opportunities for foreign investment elsewhere, multinational oil companies have begun a ‘new scramble for Africa.’” Gary claims that by the end of the decade, over \$50 billion will be spent on developing African oilfields, with production levels at seven million barrels a day by 2010 (Gary, 36). As mentioned before, the problem is that most of these African countries are unable to deal with the large revenues that come from the sale of black gold. Mismanagement and corruption run rampant, causing most of the money to be filtered into coffers that do not meet the needs of the people.

Because Chad is landlocked, it was necessary for the country and the oil consortium to develop a way to get the oil out of the country. For this, a 1,070 kilometer pipeline was built through neighboring Cameroon to the Gulf of Guinea (Bannon, 344). Funding for this pipeline was provided by the World Bank in 2000 (Oxfam 11/17/05). The World Bank, anxious to not repeat the mistakes of past projects, attached many strings to the funding for this project.

The first requirement was for Chad to set up a framework to show how the revenues of the oil would be spent. This requirement was realized in Law 001 on Petroleum Revenue Management, adopted by the Chadian government. The law reserves 80 percent of oil revenue for spending on health, social services, education, and rural development (Brannon, 346).

Among other provisions, this framework requires that the majority of royalties and dividends from oil production be earmarked and spent on poverty reduction through “priority sectors” such as health, education, and infrastructure, and that 10% of proceeds from oil sales were to be set aside in a fund for future generations in the post-oil era – an account that now contains more than \$27 million (Brannon, 346).

This framework was considered a “model” for how oil revenues could be used to meet the needs of vulnerable population sectors within a country. An independent oversight body of five external experts is to report on the process of the project and its implementation. The body is to meet twice a year, and make its findings publicly available.

However, in October 2005 the Chadian government announced that it was going to amend the law to better serve what it saw as more pressing needs. John Bray saw this move coming by 2003, when he wrote in his piece, *Attracting Reputable Companies to Risky Environments: Petroleum and Mining Companies*:

The Chad-Cameroon negotiations illustrate the strong position that companies and external lenders typically enjoy at the outset of a major project. There was no doubt that Chad needed the revenues that the project would bring, and the government was willing to accept tough conditions, including requirements for international oversight that arguably impinge on the country’s sovereignty. However, there is a risk that the politics of the “obsolescing bargain” will come into place as the project proceeds. Once the external participants have built the pipeline and other infrastructure, and therefore sunk their costs into fixed assets, the balance of power will shift in favor of the government (Brannon, 345).

The main priority for the Chadian government, rather than poverty, was security. This became clear already in November 2000, when the Chad government used part of a \$25 million oil contract bonus to purchase \$4.5 million in weapons. Some feel that a formal amendment to the law represents a great breach of trust, and a step in the wrong direction. According to a press release from Oxfam on November 17, 2005:

The planned amendment seeks to: A) increase from 15% to 30% the amount of revenues deposited into general government coffers, bypassing the joint government-civil society revenue oversight committee; B) eliminate the Future Generations Fund (FGF) and use the money accumulated for immediate expenditures; C) redefine “priority sector” expenditures to include spending on security (Oxfam 11/17/05).

Security is indeed a very important priority for the Chadian government. Social and political unrest within its own borders, as well as conflicts in neighboring African states, all affect Chad negatively. One major concern is the crisis in the Darfur region of the Sudan, which has led to thousands of refugees in Chad. Incursions by Libya in the past are also disconcerting.

However, it is very troubling that the promised spending would be siphoned away from the extreme poverty in Chad, and used to build military and security strength instead. The World Bank is also concerned by this development and released a press statement on October 25, 2005. The World Bank acknowledged that “the Government of Chad faces recurring financial problems, but [it] is concerned that addressing grave weaknesses in public financial management which the government itself has acknowledged is essential to ensuring that the poverty reduction goals of the oil revenue management program are protected (World Bank, 10/25/05).”

The funds that were provided for the development project (the most expensive in Sub-Saharan Africa’s history) were delivered under pretenses that the revenues from

the oil would be spent responsibly. Unfortunately, there is little that the World Bank, or any other entity, can do to force Chad to uphold its end of the bargain, but the oil companies are also responsible for ensuring they implement the project in a way that benefits the population and environment in Chad. This is the concept of corporate social responsibility, or CSR. If the companies are making massive profits from the exploitation of Chadian oil, it is their responsibility as well to ensure that the population of Chad is repaid in kind. The consortium of oil companies that is working in Chad is led by ExxonMobil. The company feels that it has been sensitive to the needs of the Chadian population. Miles Shaw, the public affairs adviser in Chad, states “There has been the most preparation of any oil project in Africa. We know that for a fact (Kotch 9/05).” He goes on to explain that over 6,000 village-level meetings were held in order to get the feedback of the local population, and that there were over 14,000 land owners in Chad and Cameroon who had to be negotiated with and compensated individually for the project (Kotch 9/05). Many non-governmental organizations (NGOs) remain skeptical, stating that the oil project will have a negative effect on the region’s environment and population.

This project represents an important opportunity for Exxon Mobil and the other companies to prove to the world that they can indeed work toward fostering development in their projects instead of conflict. The consortium is also in a unique position, as it alone has the power to influence the government’s decision making and policy setting processes. Instead of making contracts with the Chadian government in secret, the consortium could be using the leverage that it possesses to push forward reforms and stress adherence to the revenue management framework.

It is in the self-interest of the consortium to support these measures, as poverty and disenfranchisement are major reasons for conflict in a resource dependent country. As displayed in Nigeria, the effects of conflict in a country or region that is producing oil can be devastating to that industry. According to the annual report of Royal Dutch Shell, which pumps one million barrels of oil a day in Nigeria,

An average of 50,000 barrels a day were stolen in 2004, at a loss of almost \$1 billion. In the same period a dozen workers were killed, between 50 and 70 kidnapped, and a total of 314 criminal incidents reported. Pumping had to be halted 176 times (Thielke 12/7/05).

Instead of letting Chad use part of a consortium bonus on weapons, the consortium should be emphasizing the importance to the government of spending on poverty, health care, and education. Not only can this be used as an example in which they were socially responsible, the high costs of conflict on the industry also make this type of spending good business-sense.

For the first time in its existence, Chad is in the position to be a “model” in something. After 40 years of civil war, and enduring extreme poverty, ethnic tensions, and corruption, Chad is in the position to become a wealthy country. Spending the oil revenues in a responsible way will not only promote growth, education, and prosperity in the country, but it will also help to avoid internal conflicts and attract further foreign aid. Lenders took a big risk in this project, and if it appears to them that their goals will not be realized they will be even less likely to invest in the future. It is extremely vital that Chad stick to its original promises and policies by not amending the Revenue Management Framework law.

Because investors like the World Bank lose any sort of leverage after the infrastructure of a project is completed, it is also important that the oil companies that make up the consortium live up to their responsibilities as well. This paper has demonstrated that promoting responsible management of oil revenues is in the interest of the consortium for multiple reasons. First, it is an opportunity to show themselves to the international community as responsible stakeholders in the development process, and second it is good business-sense as well. Prevention of conflicts in Chad will prove to be less expensive in the long run for the oil consortium. The consortium should pressure the Chadian government into fulfilling its responsibility to the Chadian people, but the consortium should also live up to its own responsibilities as well.

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